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BEFORE THE ARIZONA CORPORAT

COMMISSIONERS

Arizona Corporation Commission

DOCKETED

MAY - 8 2013

BOB STUMP - Chairman
 GARY PIERCE
 BRENDA BURNS
 BOB BURNS
 SUSAN BITTER SMITH

DOCKETED BY

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IN THE MATTER OF THE APPLICATION OF
 SOUTHWESTERN TELEPHONE COMPANY FOR
 A HEARING TO DETERMINE THE EARNINGS
 OF THE COMPANY, THE FAIR VALUE OF THE
 COMPANY FOR RATEMAKING PURPOSES,
 AND TO INCREASE RESIDENTIAL RATES AS
 NECESSARY TO COMPENSATE FOR THE RATE
 IMPACTS OF THE FCC'S USF/ICC
 TRANSFORMATION ORDER.

DOCKET NO. T-01072A-12-0472

DECISION NO. 73874OPINION AND ORDER

DATE OF HEARING:

March 25, 2013

PLACE OF HEARING:

Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE:

Teena Jibilian

APPEARANCES:

Mr. Craig A. Marks, CRAIG A. MARKS, PLC, on
 behalf of Applicant; and

Ms. Maureen A. Scott, Senior Staff Counsel and Mr.
 Charles O. Hains, Staff Attorney, Legal Division on
 behalf of the Utilities Division of the Arizona
 Corporation Commission.

BY THE COMMISSION:

On November 23, 2012, Southwestern Telephone Company ("Southwestern" or "Company")
 filed with the Arizona Corporation Commission ("Commission") the above-captioned application.
 The application states that it was filed pursuant to A.R.S. § 40-250 and Arizona Administrative Code
 R14-2-103, to compensate for the rate impacts of the Federal Communication Commission's
 ("FCC's") November 18, 2011 Universal Service Fund/Inter-carrier Compensation ("USF/ICC")
 Transformation Order ("USF/ICC Transformation Order").¹

* * * * *

¹ FCC 11-161, *Connect America Fund*, WC Docket No. 10-90 et al., *Report and Order and Further Notice of Proposed Rulemaking*, 26 FCC Rcd 17663 (November 18, 2011); *pets. for review pending* (10th Cir. filed Dec. 8, 2011).

1 Having considered the entire record herein and being fully advised in the premises, the
2 Commission finds, concludes, and orders that:

3 **FINDINGS OF FACT**

4 **Procedural History**

- 5 1. On November 23, 2012, Southwestern filed the rate application with the Commission.
6 2. On January 22, 2013, Southwestern filed a Motion for Procedural Order.
7 3. On January 28, 2013, a Rate Case Procedural Order was issued, setting the matter for
8 hearing and establishing associated procedural deadlines, including the mailing of notice of the
9 application and hearing to all of Southwestern's customers.
10 4. On February 22, 2013, Southwestern filed an Affidavit regarding notice of the
11 application and hearing.
12 5. On March 25, 2013, Southwestern filed a revised Affidavit indicating that notice as
13 ordered by the Rate Case Procedural Order was mailed to each customer of Southwestern.
14 6. No requests for intervention were filed.
15 7. On March 14, 2013, Staff filed its Staff Report recommending approval of the
16 application, for an increase to \$14.00 in the monthly residence local exchange rate to address the
17 impact of the FCC's USF/ICC Order.
18 8. On March 21, 2013, Staff filed the Testimony Summary of its witness.
19 9. No public comment was filed in opposition to the rate increase.
20 10. On March 25, 2013, a hearing on the application was convened before a duly
21 authorized Administrative Law Judge of the Commission. Southwestern and Staff appeared through
22 counsel, presented testimony and evidence through witnesses, and were provided an opportunity to
23 cross examine witnesses. No members of the public appeared to provide public comment.
24 11. Following the parties' submission of evidence, the matter was taken under advisement
25 pending the submission of a Recommended Opinion and Order.

26 **Southwestern**

- 27 12. Southwestern is an Arizona public service corporation engaged in the business of
28 providing telephone utility service to the public in west central Arizona. The Company serves

1 customers in its Quartzite and Salome Exchanges. In its April 15, 2012, Utilities Annual Report,
2 Southwestern reported 1,986 residential lines and 924 business lines.

3 13. Southwestern is currently charging rates set by Commission Decision No. 63685 (May
4 24, 2001).

5 14. Southwestern is a rate of return incumbent local exchange carrier ("ILEC") eligible to
6 receive federal high-cost loop support ("FHCLS").

7 **FCC USF/ICC Order**

8 15. On November 18, 2011, the FCC issued the USF/ICC Order. The USF/ICC Order
9 provides for a transition from former federal universal service programs and most intercarrier
10 compensation systems into a new Connect America Fund ("CAF"). In its USF/ICC Order, the FCC
11 states that by July 1, 2020, intercarrier compensation rates for rate of return companies will be
12 reduced to zero. The recovery from the CAF will phase out over time at 5 percent annually.

13 16. The USF/ICC Order adds new rules that will reduce FHCLS to carriers by the amount
14 their flat-rate residential local service rates fall below a specified local service rate floor. The rate
15 floor includes state subscriber line charges, state universal service fees, and mandatory extended area
16 service charges, if any are assessed. The USF/ICC Order establishes those rate floors at \$14.00 as of
17 June 1, 2013, with the floor thereafter being determined annually by the FCC's Wireline Competition
18 Bureau.

19 17. As a recipient of FHCLS, Southwestern is affected by the FCC USF/ICC Order.
20 Under the USF/ICC Order, to continue receiving FHCLS, rural ILECs such as Southwestern must
21 increase their residential local rates to the FCC-mandated residential rate floors. Otherwise, the
22 amount of FHCLS funds received will be reduced dollar-for-dollar for each customer by the
23 difference between the existing local rate and the new rate floor.

24 **Application**

25 18. Southwestern's current rate for residential local service is \$11.25, and Southwestern
26 also serves two customers who currently have a grandfathered two-party line rate of \$9.60. The
27 application requests that Southwestern be authorized to raise all its residential local rates to the
28 \$14.00 rate floor mandated by the USF/ICC Order to allow it to continue receiving FHCLS.

1 19. Southwestern submitted the application, after consulting with Staff, in a “streamlined”
2 form. The application and accompanying exhibits in support of Southwestern’s requested increase in
3 residential rates are based on the twelve months ending June 30, 2012.

4 20. For the twelve months ending June 30, 2012, Southwestern’s filing indicates total
5 Intrastate Operating Revenues of \$1,646,758 (which includes FHCLS and Federal Safety Net
6 Additive Support of \$478,376), and total Intrastate Operating Expenses of \$1,746,502, for total
7 Intrastate Operating Income of negative \$99,744 before taxes, and negative \$60,315 after taxes.

8 21. The filing indicates a total Arizona rate base of \$4,138,383, of which \$1,572,768 is
9 interstate, and \$2,565,615 is intrastate.

10 **Staff Recommendations**

11 22. Staff states that it reviewed the application and the federal rule changes that prompted
12 its filing. Staff states that it concluded that the costs appear reasonable and appropriate under the
13 unique circumstances of this case, but that its recommendation should not be viewed as precedent for
14 the processing of future rate case applications.

15 23. Staff states that for the purposes of this proceeding, Southwestern stipulated to the use
16 of original cost less depreciation (“OCRB”) as the basis for a determination of its fair value rate base
17 (“FVRB”).

18 24. Staff reviewed and analyzed the filing, but did not perform a regulatory audit. Staff
19 does not recommend that Southwestern’s rates be set based on a revenue requirement analysis.

20 25. Staff states that the annual revenue effect of Southwestern’s requested increase in
21 local telephone service rates to \$14.00 would be \$53,368. Staff states that compared to
22 Southwestern’s total revenues, any revenue impact from this rate increase would be small, and any
23 impact on Southwestern’s fair value rate of return would be de minimus. Staff states that with
24 Southwestern’s requested increase, operating income would remain negative, and that the rate of
25 return would be less than zero, and not meaningful in this case.

26 26. Staff recommends that Southwestern’s monthly residence local exchange rate be
27 increased to \$14.00 to address the impact of the USF/ICC Transformation Order. Staff states that it
28 believes the requested increase is just, fair, and reasonable for the following reasons:

- (a) The increase is necessitated by the FCC's November 18, 2011 USF/ICC Transformation Order;
- (b) The increase is necessary to preserve the entirety of the federal USF funds that may flow to Southwestern pursuant to the FCC's rules;
- (c) The increase will minimize/reduce the amount of future rate increase; and
- (d) The increase will allow Southwestern to receive matching funds from the FUSF.

27. The Staff Report states that on November 28, 2012, the Records Section of the Corporations Division responded that Southwestern is in Good Standing, and a review of Consumer Services database revealed that no complaints, inquiries and opinions were received pertaining to Southwestern for the period January 1, 2009 – November 28, 2012.

28. Staff states that a check of the Utilities Division Compliance Section database showed that Southwestern is in compliance with all items.

Conclusions

1. Under the particular circumstances of this proceeding, a rate of return analysis is not useful.
2. According to the evidence presented, the rate increase request will have a de minimus impact on Southwestern's return on FVRB.
3. Staff's recommendations are reasonable and should be adopted.
4. Under the particular circumstances of this proceeding, all Southwestern's rates for residential local service should increase to \$14.00, and all other currently tariffed rates should remain unchanged, in order to assure continued FUSF support for Southwestern's services.

CONCLUSIONS OF LAW

1. Southwestern is a public service corporation within the meaning of Article 15 of the Arizona Constitution and A.R.S. §§ 40-250 and 40-251.
2. The Commission has jurisdiction over the Company and over the subject matter of this proceeding.
3. The Company provided notice of this proceeding in accordance with law.
4. The Company's Arizona Intrastate FVRB as of June 30, 2012, is \$2,565,615.

5. Under the particular circumstances of this proceeding, a rate of return analysis is not useful.

6. Under the particular circumstances of this proceeding, it is appropriate to increase all Southwestern's rates for residential local service to \$14.00, and to leave all other currently tariffed rates unchanged, in order to assure continued FUSF support for Southwestern's services.

7. The rates and charges authorized herein are just and reasonable and promote the public interest.

8. The Company should be directed to file revised tariffs showing the rates authorized herein.

ORDER

IT IS THEREFORE ORDERED that Southwestern Company shall increase its rates and charges in accordance with the Findings of Fact herein.

IT IS FURTHER ORDERED that such new rates and charges shall be effective for Southwestern Company's billings on or after June 1, 2013.

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1 IT IS FURTHER ORDERED that Southwestern Company is authorized and directed to file,
 2 on or before May 31, 2013, revised schedules of rates and charges consistent with the Findings of
 3 Fact and Conclusions of Law contained herein.

4 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

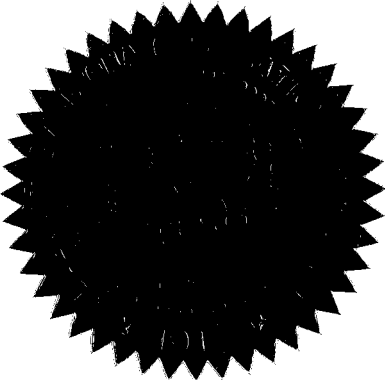
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 8 CHAIRMAN

COMMISSIONER

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COMMISSIONER



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 12 IN WITNESS WHEREOF, I, JODI JERICH, Executive
 13 Director of the Arizona Corporation Commission, have
 14 hereunto set my hand and caused the official seal of the
 15 Commission to be affixed at the Capitol, in the City of Phoenix,
 16 this 8th day of May 2013.

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 18 JODI JERICH
 19 EXECUTIVE DIRECTOR

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DISSENT

1 SERVICE LIST FOR: SOUTHWESTERN TELEPHONE COMPANY

2 DOCKET NO.: T-01072A-12-0472

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